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JUN - 3 1997

Federal Communications Commission
Office of Secretary

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket 97-__
MCI Telecommunications Co., Inc.	)	
	)	
Petition for Expedited Declaratory Ruling Preempting Arkansas Telecommunications Regulatory Reform Act of 1997 pursuant to §§ 251, 252 and 253 of the Communications Act of 1934, as amended	)	**File No. _______**

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June 3, 1997

EXECUTIVE SUMMARY

Pursuant to Sections 251, 252(e)(5), 253(d) and 254(f) of the Communications Act of 1934 as amended by the Telecommunications Act of 1996 ("the 1996 Act"), and pursuant to Section 1.1 and 1.2 of the rules and regulations of the Federal Communications Commission ("the Commission"), 47 C.F.R. §§ 1.1, 1.2 (1995), MCI Telecommunications Corporation ("MCI") hereby respectfully requests that the Commission issue a declaratory ruling preempting various provisions of the Arkansas Telecommunications Regulatory Reform Act of 1997 ("the Arkansas Act").

The Arkansas Act was passed in January 1997. The stated purpose of the Arkansas Act is to "[p]rovide a system of regulation of telecommunications services, consistent with the Federal Act, that assists in implementing the national policy of opening the telecommunications market to competition on fair and equal terms." In fact, however, the Arkansas Act erects a series of barriers to local competition that are flatly inconsistent with the requirements of federal law. It also expressly seeks to protect the revenue streams of incumbent local exchange carriers, and to protect rural telephone companies from competition.

Indeed, the very premise of the Arkansas Act is inconsistent with the national policy framework set forth in the 1996 Act. In the 1996 Act, Congress sought to ensure the opening of local markets to competition, and gave responsibility to both the FCC and to state commissions to carry out its federal mandate. The Arkansas Act seeks to strip the Arkansas commission of any power to carry out its mandate. The Arkansas Act also seeks to protect incumbent LECs -- both large and small -- from the very competition that the 1996 Act contemplated.

Numerous specific provisions of the Arkansas Act conflict with the federal regulatory framework created by the 1996 Act. MCI requests that, pursuant to § 253 of the 1996 Act, the Commission declare that the Arkansas Act's provisions relating to resale, approval of negotiated agreements and SGATs, rural telephone companies, and universal service are preempted, because they are inconsistent with the mandates of the federal Act and/or have the effect of prohibiting the ability of MCI and other telecommunications carriers to enter the local market in Arkansas. Moreover, because other provisions of the Arkansas Act prevent the Arkansas Commission from fulfilling its duties under the 1996 Act, MCI requests that this Commission preempt the Arkansas PSC's jurisdiction over all § 252 arbitrations.

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Pursuant to Sections 251, 252(e)(5), 253(d) and 254(f) of the Communications Act of 1934 as amended by the Telecommunications Act of 1996 ("the 1996 Act"), and pursuant to Section 1.1. and 1.2 of the rules and regulations of the Federal Communications Commission ("the Commission"), 47 C.F.R. §§ 1.1, 1.2 (1995), MCI Telecommunications Corporation ("MCI") hereby respectfully requests that the Commission issue a declaratory ruling preempting various provisions of the Arkansas Telecommunications Regulatory Reform Act of 1997 ("the Arkansas Act"), and preempting the Arkansas Commission's jurisdiction over § 252 arbitrations.

Section 253(d) of the 1996 Act gives the Commission the power to preempt any state "statute, regulation, or legal requirement" that "may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service," or that imposes requirements to preserve and advance universal service in a manner that is not competitively neutral. See §§ 253(a),(b),(d). The Arkansas Act does both, erecting barriers to entry that will have the effect of prohibiting the ability of MCI and other potential competitors to enter local markets in Arkansas, and imposing conditions in the name of preserving universal service that are not competitively neutral. The Commission should expeditiously exercise the power granted it under § 253(d) to preempt the Arkansas Act. These provisions of the Arkansas Act should be preempted for the further reason that they conflict directly with the requirements of § 251 of the 1996 Act and the regulations promulgated by the Commission to implement § 251, See First Report and Order, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98 (Aug. 8, 1996) ("First Report and Order"), and with the requirements of §254 of the Act, 47 U.S.C. § 214(e) and the regulations promulgated by the Commission to implement those statutory provisions. See Report and Order, In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45 (May 8, 1997) ("Univ. Svc. Order").

Furthermore, Section 252(e)(5) of the 1996 Act provides that the FCC should preempt a State commission's jurisdiction if the State commission fails to act. Because the Arkansas legislation prevents the Arkansas PUC from arbitrating interconnection agreements as required by the 1996 Act, this Commission should declare that it will preempt the State commission's jurisdiction over any Section 252 arbitration.

BACKGROUND

I. The Telecommunications Act of 1996.

In the Telecommunications Act of 1996, Congress created "a pro-competitive, de-regulatory national policy framework" for opening local telephone exchange markets to competition. S. Conf. Rep. No. 104-230, 104th Cong., 2nd Sess. 1 (1996). Recognizing that "the majority of States restrict full and fair competition in the local exchange, either by statute or through the public utility commission's regulations," H.R. Rep. No. 204, 104th Cong., 1st Sess., pt. 1, at 50 (1995), Congress preempted all state and local statutes or regulations that have the effect of prohibiting entry into any telecommunications market. See 47 U.S.C. § 253(a). Although the removal of barriers to entry is necessary to promote competition in the local market, Congress recognized that more was needed to supplant the existing local exchange monopolies. The statute thus requires incumbent local exchange carriers to offer to new entrants interconnection, unbundled network elements at cost-based rates, and all retail services at wholesale rates. See §§ 251, 252.

The Supremacy Clause mandates that federal law displace inconsistent state regulation. Federal law may preempt state law in at least three ways. First, Congress may expressly preempt state law in a particular area; second, even where Congress has not expressly so provided, an intent to displace state law in a specific area may be implied where the scheme of federal regulation is sufficiently comprehensive to make reasonable the inference that Congress left no room for supplementary state regulation; and third, state law may be preempted to the extent that it conflicts with federal law. See New York State Conference of Blue Cross and Blue Shield Plans v. Travelers Ins. Co., 115 S. Ct. 1671, 1676 (1995) (The Supremacy Clause "may entail pre-emption of state law either by express provision, by implication, or by a conflict between federal and state law"); Hillsborough County v. Automated Medical Lab., Inc., 471 U.S. 707, 712-13 (1985).

The 1996 Act, while not completely displacing state regulation, expressly provides that state regulation inconsistent with the provisions and pro-competitive purpose of the Act are preempted. Thus, § 261 provides that existing state regulations may only be enforced "if such regulations are not inconsistent with the provisions of this part," § 261(b), and new state requirements will only be permitted "as long as the State's requirements are not inconsistent with this part or the Commission's regulations to implement this part." § 261(c).

In § 253, entitled "Removal of Barriers to Entry," Congress explicitly preempted all state and local regulations that act as barriers to entry into the interstate and intrastate telecommunications markets:

> (a) IN GENERAL. -- No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.
>
> (b) State Regulatory Authority. -- Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers.
>
> . . .
>
> (d) Preemption. -- If, after notice and an opportunity for public comment, the Commission determines that a State or local government has permitted or imposed any statute, regulation, or legal requirement that violates subsection (a) or (b), the Commission shall preempt the enforcement of such statute, regulation, or legal requirement to the extent necessary to correct such violation or inconsistency.[1]

Section 253(a) preempts state requirements that operate to protect the incumbent local exchange carrier by significantly deterring or burdening potential new competitors. To

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[1]Although the 1934 Act originally established federal regulatory authority over interstate telecommunications only, these provisions and others clearly show that in the 1996 Act, Congress has re-defined the parameters of federal and state authority, extending its regulatory reach to matters that had previously been considered to be within the intrastate sphere. See Local Competition NPRM, ¶ 37-40.

"prohibit or have the effect of prohibiting" entry, a regulation need not make entry literally impossible because "a barrier may protect a market incumbent without completely excluding entry." Phillip E. Areeda, et al., Antitrust Law ¶ 420a at 57 (1995); see Los Angeles Land Co. v. Brunswick Corp., 6 F.3d 1422, 1428 (9th Cir. 1993), cert. denied, 114 S. Ct. 1307 (1994) ("The disadvantage of new entrants as compared to incumbents is the hallmark of an entry barrier.") "A barrier to entry is any factor that permits firms already in the market to earn returns above the competitive level while deterring outsiders from entering." Areeda, ¶ 420a at 55-56; see Rebel Oil Co. v. Atlantic Richfield Co., 51 F.3d 1421, 1439 (9th Cir. 1995), cert. denied, 116 S. Ct. 515 (1995) ("Barriers to entry may be defined as either additional long-run costs that were not incurred by incumbent firms but must be incurred by new entrants or factors in the market that deter entry while permitting incumbent firms to earn monopoly returns.") (internal quotes omitted).

Pursuant to § 253(b), states are given limited authority to regulate entry, but only if their requirements are (1) imposed on a competitively neutral basis; (2) necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, or safeguard the rights of consumers; and (3) consistent with the universal service requirements of § 254. If the Commission determines that a state statute violates either § 253(a) or (b), it is granted the express authority to preempt that statute. See § 253(d).

II. The Arkansas Telecommunications Regulatory Reform Act of 1997.

The Arkansas Telecommunications Regulatory Reform Act of 1997 (Arkansas Act) was passed in January 1997 (a copy is attached hereto). The stated purpose of the Arkansas

Act is to "[p]rovide a system of regulation of telecommunications services, consistent with the Federal Act, that assists in implementing the national policy of opening the telecommunications market to competition on fair and equal terms." In fact, however, the Arkansas Act erects a series of barriers to local competition that are flatly inconsistent with the requirements of federal law. It also expressly seeks to protect the revenue streams of incumbent local exchange carriers, and to protect rural telephone companies from competition.

III. Preempted Provisions of the Arkansas Act.

The very premise of the Arkansas Act is inconsistent with the national policy framework set forth in the 1996 Act. In the 1996 Act, Congress sought to ensure the opening of local markets to competition, and gave responsibility to both the FCC and to state commissions to carry out its federal mandate. The Arkansas Act seeks to strip the Arkansas commission of any power to carry out its mandate. The Arkansas Act also seeks to protect incumbent LECs -- both large and small -- from the very competition that the 1996 Act contemplated.

Numerous specific provisions of the Arkansas Act conflict with the federal regulatory framework created by the 1996 Act. MCI requests that the Commission declare that the following provisions are preempted, because they are inconsistent with the mandates of the federal Act and/or have the effect of prohibiting the ability of MCI and other telecommunications carriers to enter the local market in Arkansas.

A. The Restrictions on Purchasing Service for Resale of Section 9(d) and the Wholesale Rates Set for Resale Services of Section 9(g) are preempted.

The restrictions on purchasing services for resale imposed by §§9(d) and 9(g) of the Arkansas Act are preempted by the 1996 Act because they constitute barriers to entry in violation of §253 and because they directly conflict with the commands of §251(c)(4) and the

First Report and Order.

Section 9(d) of the Arkansas Act denies competing carriers the ability to obtain "[p]romotional prices, service packages, trial offerings or temporary discounts offered by the local exchange carrier to its end-user customers" for resale. Thus, under the terms of the Arkansas Act, CLECs offering service through resale cannot purchase at wholesale rates any service the ILEC deems promotional. Nor can they purchase at wholesale rates any service the ILEC bundles with other services as a "package."

This prohibition on resale is in direct conflict with the Act and the First Report and Order. The Act requires that incumbent LECs "offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers." § 251(c)(4). Citing this requirement, the Commission found that "no basis exists for creating a general exemption from the wholesale requirement for all promotional or discount service offerings made by incumbent LECs." Order at ¶ 948.

The Commission also recognized that "a contrary result would permit incumbent LECs to avoid the statutory resale obligation by shifting their customers to nonstandard offerings." Id. Because a CLEC offering service through resale cannot effectively compete with ILECs unless they can obtain the service at a wholesale rate, and are therefore able to market the service to consumers at a competitive rate, the Arkansas Act's prohibition on the resale of promotional offerings would allow ILECs to stave off competition by designating their retail service offerings "promotions." To avoid this anti-competitive result, the Commission specifically found that, with the exception of "short-term" promotions of 90 days or less, ILECs must offer promotional or discount offerings for resale at wholesale rates. Id. The Arkansas

Act's mandate that promotional offerings need not be offered for resale cannot be reconciled with the requirements of federal law.

Similarly, the method by which the Arkansas Act directs the state commission to calculate wholesale discounts cannot be reconciled with the requirements of the 1996 Act. Section 9(g) of the Arkansas Act requires the "wholesale rate" to be calculated by subtracting from the retail rate "any net avoided costs." Net avoided costs are defined as the sum of the costs "that will not be incurred by the local exchange carrier due to it selling the service for resale less any additional costs that will be incurred as a result of selling the service for the purpose of resale." Id. Thus, when setting wholesale rates, the Arkansas Act requires ILECs to subtract from the retail rate any costs not incurred when the service is offered for wholesale, but also allows the ILEC to add to retail rates any costs allegedly incurred when the relevant service is sold at wholesale.

The 1996 Act, by contrast, dictates that wholesale rates be set "on the basis of retail rates . . . excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier." 47 U.S.C. § 252(d)(3). The statute does not allow for any consideration of additional costs that are purportedly incurred when the ILEC sells services at wholesale rates for resale. The Arkansas legislature's attempt to graft further requirements onto the 1996 Act is simply not permissible.

B. The Arkansas Act's Requirement that Negotiated Agreements and SGATs be Automatically Approved is Preempted.

Section 9(I) of the Arkansas Act requires the state commission to "approve any negotiated interconnection agreement or statement of generally available terms unless it is shown by clear and convincing evidence that the agreement or statement does not meet the minimum requirements of Section 251 of the Federal Act." This provision is contrary to the requirements of the Federal Act, and should be preempted.

The Federal Act sets out the standards that govern when state commissions review statements of generally applicable terms (SGATs). Specifically, the statute provides that state commissions "<u>may not approve</u> such statement unless such statement complies with subsection (d) of this section <u>and</u> section 251 <u>and</u> the regulations thereunder." § 252(f)(2) (emphasis added). The Arkansas Act violates this requirement in several ways. First, it only allows the commission to reject an SGAT if the SGAT does not meet the requirements of § 251 of the Federal Act. This precludes the commission from considering whether the SGAT meets the requirements of § 252(d) or applicable regulations, as the Act requires.

The Arkansas Act also impermissibly alters the level of scrutiny required by the 1996 Act for SGATs. The Federal Act dictates that a state commission must <u>reject</u> the SGAT unless it finds that the statutory requirements are met. Thus, Congress clearly intended for commissions to scrutinize SGATs closely, and refuse to accept them unless every relevant federal requirement was met. By contrast, the Arkansas Act requires the commission to <u>accept</u> the SGAT unless it can demonstrate by <u>clear and convincing evidence</u> that it violates § 251. This is facially incompatible with the requirements of the Federal Act, reversing the level of scrutiny Congress demanded.

The Arkansas Act is also inconsistent with the requirements of the Federal Act with respect to state commission review of negotiated agreements. Under the 1996 Act, state commissions must scrutinize such agreements and reject them if the agreement discriminates against a telecommunications carrier who is not a party to the agreement, or if implementation of the agreement is not consistent with the public interest, convenience or necessity. § 252(e)(2)(A). The Federal Act clearly contemplates real scrutiny of negotiated agreements, and does not allow for approval of a negotiated agreement unless it can be demonstrated by "clear and convincing evidence" that it should not be approved. Accordingly, the Commission should declare that these provisions are preempted.

C. The Arkansas Act's Provisions that Relate to Rural Telephone Companies are Preempted.

Section 10 of the Arkansas Act exempts rural telephone companies[2] from the requirements of Sections 251© and 252 of the 1996 Act, including the duty to allow access to unbundled network elements, the duty to interconnect, or the duty to provide physical collocation, unless a number of specified criteria are met. The criteria established by the Arkansas Act, and the burden of proof associated with those criteria, are flatly inconsistent with both the requirements and the purpose of the 1996 Act and the First Report and Order, and should therefore be preempted.

The 1996 Act provides an exemption from the requirements of Section 251© to rural telephone companies only until the rural telephone company receives a bona fide request for interconnection. At that point, the state commission must determine whether the request is

[2] The Act defines "rural telephone company" as "a local exchange carrier defined as a rural telephone company in the Federal Act . . ." Section 3(20). The Federal Act defines rural telephone company as a local exchange carrier that: "(A) provides common carrier service to any local exchange carrier study area that does not include either -- (I) any incorporated place of 10,000 inhabitants or more . . .; or (ii) any territory, incorporated or unincorporated, included in an urbanized area . . .; (B) provides telephone exchange service, including exchange access, to fewer than 50,000 access lines; © provides telephone exchange service to any local exchange carrier study area with fewer than 100,000 access lines; or (D) has less than 15 percent of its access lines in communities of more than 50,000 on the date of enactment of the Telecommunications Act of 1996." 47 U.S.C. § 153(37).

not unduly economically burdensome, is technically feasible, and is consistent with the universal service provisions found in § 254 of the 1996 Act. If the request meets these criteria, the state commission is directed to remove the exemption. The 1996 Act provides for no other criteria that can be considered by a state commission in determining whether the exemption should be retained.

In allowing for this limited exemption, Congress did not "intend to insulate smaller or rural LECs from competition, and thereby prevent subscribers in those communities from obtaining the benefits of competitive local exchange service." Order at ¶ 1262. Indeed, as this Commission found, exemption should be "the exception rather than the rule." Id. Accordingly, this Commission established clear rules that state commissions must apply in determining whether a rural telephone company may retain its exemption in the face of a bona fide request for interconnection. These rules are designed to prevent rural telephone companies from insulating themselves from competition unless they can demonstrate that such protection is clearly warranted.

Thus, for example, because any competition will presumably result in a rural telephone company realizing less revenue than it would as a monopoly provider of phone service, a rural telephone company requesting continued exemption on the ground that interconnection would be "unduly economically burdensome" must demonstrate that, without continued exemption, it would suffer "economic burdens beyond the economic burdens typically associated with efficient competitive entry." Order at ¶ 1262; 47 C.F.R. § 51.405. Moreover, the burden to demonstrate that one of the three statutory criteria that justify exemption exists is placed squarely on the rural telephone company. "[R]ural LECs must prove to the state commission that they should continue to be exempt pursuant to section 251(f)(1) from requirements of section 251(c). . . ." Order at ¶ 1263 (emphasis added); 47 C.F.R. § 51.405.

In sharp contrast to the 1996 Act and the First Report and Order, the Arkansas Act seeks to protect rural telephone companies from competition by altering the burden of proof set forth in the First Report and Order, and imposing additional requirements that must be met before a rural telephone company is required to provide interconnection. For example, although the Federal Act requires the rural telephone company to justify continued exemption by proving that one of the three statutory criteria cannot be met, the Arkansas Act forbids the state commission from removing an exemption unless it is established by clear and convincing evidence that the request is not economically burdensome, that the request is technically feasible, and that the request is consistent with the protection of universal service and the public interest, convenience, and necessity.[3] Section 10(b).[4] The Arkansas Act thus shifts the burden to requesting carriers, and requires them to demonstrate by clear and convincing evidence -- a standard not found in the Federal Act or regulations -- that removal of the exemption is warranted.

Moreover, the Arkansas statute dictates that the commission may not conclude that the "clear and convincing" standard has been met unless ten additional factors can be

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[3] Although this language roughly mirrors the Federal Act, it imposes an additional requirement that removing the exemption be consistent with the public interest, convenience and necessity.

[4] This Section of the Arkansas Act applies to non-"Tier One" companies. The Arkansas Act defines a Tier One company as an "incumbent local exchange carrier that, together with its Arkansas affiliates that are also incumbent local exchange carriers, provides basic local exchange services to greater than one hundred fifty thousand (150,000) access lines in the State of Arkansas . . . ." Section 3(26).

satisfied, a number of which are unquestionably designed to protect the local rural monopoly.[5] Neither the Federal Act nor the Commission's Order contemplates or allows states to impose additional factors that must be met before an exemption is removed. The Arkansas Act is therefore flatly in conflict with the Federal law and clearly "may prohibit or have the effect of prohibiting the ability of any entity" from providing local service in competition with the rural ILEC. The FCC should accordingly exercise its § 253(d) authority and preempt this portion of the statute.

D. The Arkansas Act's Provisions Related to Universal Service are Preempted.

The Universal Service provisions in Sections 4 and 5 of the Arkansas Act are preempted by the 1996 Act because they constitute barriers to entry in violation of §253 and because they directly conflict with the commands of §§214(e) and 254 of the 1996 Act and this Commission's Universal Service Order.

Section 4 of the Arkansas Act is titled "Preservation and Promotion of Universal Service." In fact, however, the Arkansas Act does not promote universal service but instead impermissibly attempts to preserve revenue streams for incumbent local exchange carriers in violation of the 1996 Act. For example, Section 4(e)(4)(A) of the Arkansas Act provides that "[i]n the event of an FCC order, rule or policy . . . the effect of which is to change the federal

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[5] The commission must find that granting the bona fide request will not adversely impact: "1) The customers of the incumbent local exchange carrier serving the area; 2) The incumbent local exchange carrier's ability to provide its customers adequate service at reasonable rates; 3) The incumbent local exchange carrier's ability to continue to meet eligible carrier obligations; 4) Statewide average toll rates; 5) Customers cost of telephone service; 6) The goals of universal service; 7) The quality of service provide to customers; 8) The incumbent local exchange carrier's ability to attract capital and incur debt at reasonable rates and the ability to sustain sufficient revenue stream to pay existing debt; 9) The Ability of the exchange to support more than one local exchange carrier; and 10) The interest of all ratepayers. Section 10(c).

universal service fund revenue of an incumbent local exchange carrier, the Commission shall either increase the rates for basic local exchange service or increase the incumbent local exchange carrier's recovery from the [Arkansas Universal Service Fund] or a combination thereof to replace the reasonably projected change in revenues." Thus, the Arkansas Act guarantees incumbent LECs the same level of federal universal service funding which they received prior to passage of the 1996 Act and universal service reform.

This, however, conflicts with the 1996 Act. The 1996 Act expressly removed hidden subsidies, and mandated that a mechanism be established by which universal service funding is equitable, nondiscriminatory and competitively neutral. See § 254; Univ. Svc. Order at ¶¶ 47-48. Section 4 of the Arkansas Act ensures that ILECs will continue to receive the same amount they have historically received in universal service funding, even if, under the 1996 Act and the Commission's Universal Service Order, they are not entitled to do so. No provision is made for their competitors to receive additional funding, even if they are identically situated to the ILEC.

Moreover, the Arkansas Act specifically precludes conditioning receipt of funding on "any rate case or earnings investigation." Section 4(e)(4)(C). Thus, the Act expressly precludes considerations of cost when calculating universal service funding received by ILECs under this Section. This is flatly incompatible with the Federal Act's requirement that such calculations be based on cost. See Univ. Svc. Order at ¶¶ 224-231.

Section 4 also requires the state commission to calculate the amount of universal service funding using "all net investment, including embedded costs . . ." Section 4(e)(5). This Commission has made clear, however, that the proper cost methodology to use is forward looking costs which, by definition, do not include embedded costs. See Univ. Svc. Order at ¶ 227. Indeed, in its Universal Service Order, this Commission expressly rejected consideration of embedded costs in setting universal service subsidy rates. See id. ("[W]e conclude that the universal service support mechanism should be based on forward-looking economic cost, and we reject the arguments for basing the support on a carrier's embedded costs."). Because this provision of the Arkansas Act is flatly inconsistent with the requirements of Federal law, it is preempted.

Section 5 of the Act is also preempted. Section 5 of the Arkansas Act delineates which carriers are eligible to receive universal service funding. That Section deems the ILEC the eligible telecommunications carrier within a service area, whether or not it meets the requirements of the Federal Act. That Section also provides that other carriers may be designated "eligible telecommunications carriers" in a given service area, but only if they meet five separate requirements. These requirements include: 1) the telecommunications carrier provides services to all customers in an ILEC's service area using its own facilities or a combination of facilities and resale; 2) funding is available only for facilities actually owned by the requesting carrier; 3) funding cannot be received at a level higher than that received by the ILEC; 4) the availability of service must be advertised, and; 5) designation of the requesting carrier as an eligible carrier must be in the public interest.

This provision is in direct conflict with the 1996 Act in a number of ways. First, to be eligible for funding any carrier, including the ILEC, must meet the requirements of the 1996 Act. There is no provision allowing the incumbent local exchange carrier to receive automatic entitlement to funding, while competing carriers must seek approval. Moreover, the

1996 Act requires other carriers to be deemed eligible for universal service support if they meet the requirements set out in the 1996 Act. The Arkansas Act, by contrast, impermissibly makes the eligibility determination optional.

Second, and more fundamentally, the Arkansas Act imposes requirements beyond those found in the 1996 Act that non-rural carriers must meet to qualify for funding. The Federal Act clearly and specifically delineates the conditions a carrier must meet to be eligible for universal service funding. These are: 1) that the carrier "offer the services that are supported by Federal universal support mechanisms . . . either using its own facilities or a combination of its own facilities and resale of another carrier's services"; and 2) that the carrier "advertise the availability of such services." 47 U.S.C. § 214(e)(1). "[S]ection 214(e)(2) does not permit the Commission or the states to adopt additional criteria for designation as an eligible telecommunications carrier." Univ. Svc. Order at ¶ 135; see also id. ("The statute does not permit . . . a state commission to supplement the section 214(e)(1) criteria that govern a carrier's eligibility to receive federal universal service support."). Thus, any state requirement that goes beyond the two requirements of § 214(e)(1) is inconsistent with the Act and must be preempted.

The Arkansas Act clearly does go beyond the federal requirements -- imposing five criteria instead of the two contained in the 1996 Act. For example, the Arkansas Act requires that a carrier receive funding only for facilities that it actually "owns." This Commission has made clear that a carrier is eligible for funding if it provides "service through unbundled network elements." See Univ. Svc. Order at ¶ 164. The Arkansas Act's requirement that a carrier "own" facilities before it can receive funding cannot be reconciled with the Federal Act and this Commission's Universal Service Order.

Similarly, the Arkansas Act's requirement that the competing local exchange carrier not receive universal service funding at a level higher than that received by the ILEC is inconsistent with the 1996 Act and is a flagrant attempt to preserve revenue streams of the incumbent LEC. This Commission has determined that a forward-looking cost methodology is the appropriate methodology to employ in setting funding levels. See Univ. Svc. Order at ¶¶ 224-231. The level of funding must be set with reference to a cost study and cannot depend on the identity of the carrier. The Arkansas Act's attempt to circumvent this clear requirement by ensuring that the ILEC always receives the highest level of funding is preempted.

Finally, the Arkansas Act's requirement that a competing carrier be denied universal service funding unless the state commission finds that to do so would be in the public interest is also in conflict with the 1996 Act. The 1996 Act requires state commissions to designate non-rural competing carriers as eligible for universal service funding if the two requirements laid out in § 214(c)(1) are met. The Act does not allow the state to require the state commission to consider additional factors when making this determination. In fact, this Commission considered and expressly rejected the argument that states can make a "public interest" determination when deciding whether carriers are eligible for universal service funding in non-rural areas. See Univ. Svc. Order at ¶ 135 (explaining that state commissions can take the "public interest" into account only when deciding whether to designate more than one eligible carrier in a rural area).

Section 5 of the Arkansas Act violates the 1996 Act in yet another respect. Section 5(d) of the Arkansas Act designates incumbent rural telephone companies as the only carriers eligible for universal service funding in their rural areas. The Arkansas Act thus precludes the state commission from designating a competitor in a rural area. By contrast, the 1996 Act allows designation of competing carriers in rural areas if the two conditions outlined above are met, and if the state commission determines that designating a competing carrier serves the public interest. 47 U.S.C. § 214(e)(2). Because the universal service provisions of the Arkansas Act conflict with the 1996 Act, this Commission should declare that they are preempted.

IV. The Arkansas Act's Restrictions on the Power of the Arkansas Commission Prevents the Arkansas Commission from Fulfilling the Requirements of the Federal Act, and this Commission Should Therefore Declare that the Arkansas PSC's Authority Over Section 252 Arbitrations is Preempted.

Section 9(d) of the Arkansas Act prohibits the Arkansas state commission from fulfilling its duties under the 1996 Federal Act and this Commission's Order. The Federal Act contemplates a partnership between the FCC and state utilities commissions, in which the FCC sets binding national rules and states carry out, and supplement, in accordance with the 1996 Act, those requirements. For example, in its Order, the FCC established a minimum list of network elements that are "technically feasible" to unbundle and which, therefore, ILECs must provide to requesting CLECs as unbundled network elements. However, in order to implement § 251's requirements, the Commission also specifically directed state commissions to require further unbundling of an ILEC's network if the state commission finds that such unbundling is technically feasible. Thus, the Commission found that the Act and the Order serve as a floor, not a ceiling, and that state commissions should, consistent with the Act and the Order, impose additional obligations on ILECs if doing so is consistent with the 1996 Act, and furthers the goals of the Act.

The Arkansas Act, however, prohibits the Arkansas Commission from ordering any further unbundling or opening up of the ILEC's network to competition, directing it "not to require an incumbent local exchange carrier to negotiate resale of its retail telecommunications services, to provide interconnection, or to sell unbundled network elements to a competing local exchange carrier for the purpose of allowing such competing local exchange carrier to compete with the incumbent local exchange carrier in the provision of basic local exchange service," except as expressly required by the Federal Act. Section 9(d). Thus, despite the fact that the 1996 Act and the First Report and Order anticipate state commissions' continuing involvement in the process, this Section effectively prevents the Arkansas commission from imposing any additional requirements on the ILECs, impeding the process of opening local markets in Arkansas.

The Arkansas Act also expressly restricts the state commission's power with respect to interconnection, resale, and unbundling to the "terms, conditions and agreements pursuant to which an incumbent local exchange carrier will provide interconnection, resale or unbundling to a CLEC for the purpose of the CLEC competing with the incumbent local exchange carrier in the provision of telecommunications services to end-user customers." Section 9(f). Thus, the Arkansas Act strips the commission of the authority to act with respect to anything other than contract terms contained in agreements between incumbent LECs and potential competitors relating to interconnection, resale and unbundling.

The 1996 Act allows no such restriction. As set out above, §§ 251 and 252 of the Act and this Commission's Order vest in state commissions the responsibility to determine whether the unbundling of requested elements is technically feasible, § 251(c)(3); to calculate, consistent with the Federal Act, the cost for such unbundled elements, § 252(d); to calculate, consistent with the Federal Act, the wholesale discount at which services will be sold for resale, § 251(c)(4), to determine whether a rural telephone company is exempt from certain of the Act's requirements, § 251(f)(1)(A); to review and approve or disapprove negotiated agreements, § 252(e)(2); to arbitrate, upon the request of a party, <u>any</u> open issue arising out of a request for interconnection, services, or access to unbundled elements -- including any issue necessary to reach a final agreement, § 252(b); to review and approve or disapprove such arbitrated agreements, § 252(e)(2); and to review and approve or disapprove statements of generally available terms (SGATs) filed by a Bell operating company pursuant to § 252(f), § 252(f)(2).

As a result of these restrictions, the Arkansas Public Service Commission cannot carry out its responsibilities under § 252 of the 1996 Act. The State of Arkansas, of course, has the right to determine the subjects its Public Service Commission may address. However, in restricting the scope of the Arkansas PSC's authority in these ways, the State has made it impossible for the PSC to carry out the function entrusted to it by Congress in the 1996 Act. For example, the PSC cannot, consistent with state law, require additional unbundling beyond that prescribed in the <u>First Report and Order</u>, even if that unbundling would be required by the general requirements of § 251 of the 1996 Act. Thus, the Commission must either conclude that these restrictions on the scope of the PSC's authority are preempted, or must declare that the PSC cannot carry out its responsibilities under the Act in light of the restrictions on its authority imposed by Arkansas law. Because it is not entirely clear that Congress can override the decision of a State to restrict the authority of its public service commission, the latter course provides a more secure means to ensure that the specific requirements and general policies of the 1996 Act are implemented in Arkansas.

CONCLUSION

A number of specific provisions of the Arkansas Act are preempted because they conflict with the express requirements of the 1996 Act and this Commission's Orders, and because they constitute a barrier to entry under § 253 of the 1996 Act. The Commission should therefore declare that these provisions are preempted.

Other provisions limit the power of the state commission in a way which prevents it from carrying out its responsibilities under the 1996 Act. Accordingly, this Commission should declare that pursuant to § 252 (e)(5) it will preempt the Arkansas state commission's jurisdiction over any § 252 arbitration or similar proceeding, and will assume the responsibility of the state commission in such proceeding.

Respectfully submitted,

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